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VIA EMAIL ONLY

August 7, 2018

Mr. Carsten Beith
Managing Director
Cain Brothers
601 California Street, Suite 1505
San Francisco, CA 94108

Dear Mr. Beith:

We are pleased to provide this non-binding indication of interest of Prospect Medical Holdings, Inc. ("Prospect") with respect to a proposed transaction in which Prospect, or a designated subsidiary, would acquire substantially all of the assets (as described in the Confidential Information Memorandum) of Verity Health Systems of California, Inc. and its subsidiaries ("Verity" or the "System"). The following represents the basic framework of our proposal and, if acceptable to Verity shall serve as a basis for a more formal Asset Purchase Agreement ("APA").

Pursuant to your request, the following are responses to the questions posed in your request for a proposal.

1. Organization Overview

Prospect is an innovative healthcare service delivery company that is responding to the evolving healthcare environment through meaningful collaboration among physicians, hospitals and other providers in the health care continuum. Prospect's proven track-record with hospital integration and growth is directly related to its collaborative and cooperative relationships with physicians to promote the quality and efficiency of patient care. Prospect believes that it will meet the proposed transaction's objectives due to its financial strength, its proven population health management infrastructure and its strong management team of seasoned operating, marketing, contracting, financial and



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administrative executives who maintain a dedicated “*hands-on*” commitment to the delivery of quality, cost effective healthcare services.

Prospect provides quality, cost-efficient and coordinated healthcare services through our hospitals, clinics and physician networks in Southern California, Connecticut, New Jersey, Pennsylvania, Rhode Island and Texas.

We conduct our business operations through three complementary segments: the hospital segment, population health through individual practice association (IPA) ownership and management; and primary care clinics, and specialty and outpatient facilities and services. These business segments have operated on three performance drivers – efficiency, volume and quality. Through our hospital segment, we own and operate 20 acute care and behavioral hospitals, with a total of approximately 3,790 licensed beds, and a network of 165 specialty and primary care clinics. Prospect employs over 750 physicians.

Our hospitals are located in diverse population areas. All of our facilities provide a comprehensive range of services tailored to meet the needs of their specific communities, and our collaborative relationships include other area hospitals, physicians and health plans. We believe that our proven model has several competitive advantages, including a data-driven and cost-efficient platform that has enabled us to provide efficient and quality care to patients.

Many of our hospitals in Southern California are considered safety net hospitals. In fact, we are a member of Private Essential Access Community Hospitals (“PEACH”). PEACH is a network of private, core safety net hospitals in California that care for a disproportionate share of low-income, medically vulnerable patients. Despite increased need for services, declining revenues and a host of other challenges, Prospect remains dedicated to the mission of providing choice and access to high quality, culturally appropriate, and cost-effective health care services to all patients, regardless of ability to pay.

Through our medical group segment, we manage the provision of physician services to approximately 450,000 enrollees of Health Maintenance Organizations (“HMOs”) through a network of approximately 11,000 affiliated primary care and specialty physicians. Based on our enrollment, our medical groups have a significant presence in Southern California and have long-term capitated contracts with nearly all major HMOs operating in the region. We have established Accountable Care Organizations in Connecticut and Rhode Island and participate in a CMS established alternative payment model in Pennsylvania.

We operate both our facilities and medical groups by applying highly disciplined, data-driven management to the provision of quality care to our patients. Through the in-depth analysis and application of various operational and financial metrics, we have been able to achieve a highly efficient cost structure across a diverse mix of payers and have been able

to adapt to economic and regulatory changes. We believe the most cost-efficient and quality driven providers will succeed in this rapidly changing economic and regulatory environment. Furthermore, we believe the coordination of our facilities and medical groups creates an efficient healthcare delivery system that positions us well for the future of healthcare delivery.

Prospect currently owns and operates the following hospital facilities:

- Los Angeles Community Hospital;
- Southern California Hospital at Van Nuys;
- Los Angeles Community Hospital at Norwalk;
- Southern California Hospital at Hollywood;
- Southern California Hospital at Culver City;
- Foothill Regional Medical Center;
- Los Angeles Community Hospital at Bellflower;
- Nix Medical Center;
- Nix Specialty Health Center;
- Nix Behavioral Center;
- Roger Williams Medical Center;
- Our Lady of Fatima Medical Center;
- Rockville General Hospital;
- Manchester Memorial Hospital;
- Waterbury Hospital;
- East Orange General Hospital;
- Crozer-Chester Medical Center;
- Springfield Hospital;
- Taylor Hospital; and
- Delaware County Memorial Hospital.

Our operating model is to have a strong and quality driven hospital or clusters of hospitals in a region; build and support physicians and medical groups through a menu of alignment models around those hospitals; and develop what we call a Coordinated Regional Care Platform (“CRCP”). In addition to hospitals and physicians, the CRCP involves the entire continuum of patient care including home health, clinics, independent physicians, nursing homes, ambulatory surgical centers, out-patient diagnostic services and other health care related services. What distinguishes Prospect in the marketplace is its proven ability to effectively and profitably manage risk, capitation, and bundled payments on behalf of our hospitals and medical groups while at the same time delivering a high quality of care. This unique structure allows managed care plans to focus on marketing; physicians to focus on patient care; and Prospect to coordinate medical management that ensures quality and efficiency.

Prospect currently employs approximately 750 physicians. As healthcare reform focuses on quality care delivered efficiently, Verity is well positioned; and with Prospect's capital, experience in value-based care and population health management, and additional resource commitments, Verity will have an enhanced ability to continue to provide quality healthcare to its surrounding communities.

Our interest in Verity is based on its history of providing quality care, its strong market presence and commitment to its local communities, its reputation and the quality of its medical staff and what we believe is its significant potential for growth by implementing a CRCP strategy. We believe that this is the right opportunity for Prospect and plan to build upon Verity's significant achievements as an essential community system.

As a national leader in owning and operating systems which provide value-based care, we believe that Verity and Prospect are a perfect fit for each other. Prospect's goal as a company is to continually grow and enhance our population health management in existing markets. Verity is a leading healthcare provider in its markets that has accumulated all the assets necessary to undertake population health management through its development of physician practices and outpatient services.

2. Form of Transaction.

We propose to form one or more new entities to purchase substantially all the tangible and intangible assets owned or used by Verity as such assets are described in the Confidential Information Memorandum ("CIM") in its operations and included in the APA (*Please see "Appendix A" for proposed balance sheet allocation schedule.*) We will not acquire the assets or liabilities of Marillac Insurance Company Ltd. We contemplate that the assets would be conveyed and assigned free and clear of all liens, claims, charges or encumbrances other than (i) easements, rights of way, restrictions and other matters that do not materially affect the use or value of the assets, and (ii) such encumbrances expressly assumed by Prospect in the definitive documents.

Prospect will not assume any liabilities (including any liabilities relating to deferred management fees, long-term debt, notes payables, lines of credit, capital lease obligations, pension liabilities and related party obligations) except for (i) operating accounts payable and accruals incurred in the normal course of business in accordance with generally accepted accounting principles or (ii) other liabilities specifically assumed by Prospect as set forth in the definitive documents.

Using Verity's available cash (as represented by financial statements and other information provided in the CIM and the data room, which generally exclude all assets of the various Verity Foundations and Marillac assets and liabilities – other than excess assets of Marillac) of approximately \$128,399,000 (which includes Marillac excess cash)

supplemented by Prospect cash at closing, we propose to pay all the following liabilities in exchange for all of the System assets:

A. Series 2005 A Bonds	\$246,345,000
B. Series 2005 G Bonds	\$ 10,885,000
C. Series 2005 H Bonds	\$ 8,985,000
D. Series 2015 A Notes	\$ 60,000,000
E. Series 2015 B Notes	\$ 45,000,000
F. Series 2015 C Notes	\$ 10,000,000
G. Series 2015 D Notes	\$ 45,000,000
H. Series 2017 A Notes	\$ 21,000,000
I. Series 2017 B Notes	\$ 21,000,000
J. Series 2017 MOB Notes	\$ 46,220,000
K. Series 2018 MOB Notes	\$ 15,000,000
L. 15% pro rata to unsecured creditors (other than deferred management fee)	\$ 12,000,000
M. Estimated Verity tail insurance cost	\$ 45,000,000
N. Estimated Verity transaction cost	<u>\$ 20,000,000</u>
	<u>\$606,435,000</u>

Based on Verity's May 2018 Balance Sheet, Prospect cash at close is expected to be approximately \$501 million. Given the seismic and critical maintenance requirements estimated at over \$127 million, the total value of our transaction is approximately \$628 million. To the extent that Prospect is able to assume any long-term liabilities, the amount of cash to be paid by Prospect at closing shall be reduced dollar-for-dollar by the amount of liabilities assumed.

All future California Quality Assurance Fees received by the System from the date of this indication of interest until the closing of the transaction shall be applied to the payment of secured long-term of the System prior to payment for any management fees, related party payables or unsecured debt.

If Verity believes that value can be maximized through a Section 363 bankruptcy or other insolvency proceeding, we propose a stalking horse bid for the Verity assets with the parameters stated above. We would also propose a break-up fee of three percent (3%) of the total value of our transaction in the event of a stalking horse bid.

The above schedule of secured debts was prepared with the following additional assumptions communicated to us by Cain Brothers:

- (i) No amount has been drawn on the PACE bonds
- (ii) There are no additional penalties and / or premiums due resulting from the pre-payment of debt described above.

3. Source of Financing.

Prospect will fund this transaction and all of its commitments through a combination of cash on hand, debt and equity. The closing of this transaction will not be subject to a financing contingency.

4. System Executive Leadership and Hospital Executive Leadership.

Prospect expects to offer employment, subject to customary pre-employment screenings, to substantially all employees of Verity, including respective management at the System and Hospital level who are active, and in good standing, at the time of the closing of the transaction. We also expect to continue to provide competitive salaries and benefits to Verity's employees. Furthermore, seniority levels of employment will be honored

5. Operations.

We will endeavor to further strengthen Verity's healthcare delivery model with the goal of providing high quality care in a coordinated, efficient manner throughout the communities served by Verity. We plan to enhance Verity's existing capabilities as necessary and appropriate, in areas related to accountable care, and clinical integration with physicians and other providers.

Finally, implementing the CRCP model aligns physicians with the health system and measures the improvement in population health management and positions our regional systems for success under value-based, risk contracts with payers. We integrate processes between the hospitals and its aligned physicians under those value-based contracts with payers that measure, manage and improve quality, utilization and efficiency metrics.

As such, we intend to invest in Verity's infrastructure and to develop scalable tools and technology to effectively manage the health of the population served by Verity. It is our goal that Verity not only remains viable but becomes the market leader in providing high safety and quality healthcare services at low cost to the community for the long-term. We will endeavor to form an integrated healthcare delivery model which will necessarily involve a physician engagement strategy with the goal of providing high quality care in an efficient manner. We plan to implement, as necessary and appropriate, health reform required changes including, but not limited to: value-based payment, bundled payment, accountable care, and clinical integration with physicians and other providers.

We do not anticipate any changes to the medical staff at the hospitals. In fact, we would work with the members of the medical staff in order to garner their support for this transaction. Prospect will commit to continued membership and privileges for current members of the medical staff and its leadership.

Prospect will work with medical staff at the Verity hospitals to ensure that physicians maintain an active presence at the facilities and are kept informed and provided with

necessary assistance during the transition planning phase and are encouraged to maintain their medical practices within the community.

6. Collective Bargaining Agreements.

Prospect does not intend to assume Verity's multi-employer plan or single employer plan obligations. As such the collective bargaining agreements must, at a minimum, be amended to reflect that Employer (as such term is defined in the collective bargaining agreements) will no longer provide such benefits. Further changes may be requested.

7. Post-Retirement Obligations

Prospect does not intend to assume Verity's multi-employer plan or single employer plan obligations.

8. Required Approvals

This indication of interest has been approved by Prospect's senior management team. The consummation of the proposed business combination shall be subject to and contingent upon each of the following being satisfied:

- (i) The execution of a mutually satisfactory Definitive Agreement, which agreement shall contain, among other things, such covenants, conditions, representations and warranties, indemnifications, ancillary agreements thereto and other provisions customarily found in such an agreement;
- (ii) Completion and satisfaction of the results of due diligence conducted by Prospect in its sole discretion (which shall be a condition to the execution of the Definitive Agreement);
- (iii) The approval of the transaction by each of the parties' respective governing boards, in their discretion (which shall be a condition to the execution of the Definitive Agreement); and
- (iv) Receipt by the Parties of any necessary governmental consents or third-party approvals to consummate the transaction.

9. Due Diligence

We anticipate conducting final confirmatory due diligence and negotiating Definitive Documents along a parallel path. Assuming timely receipt of the requested information, we anticipate that final confirmatory diligence and execution of the definitive documents will occur within 45 to 60 days. We would then close the transaction as soon as possible after receiving the necessary regulatory approvals.

10. **Contingencies**

None

11. **Key Contacts**

We have not yet hired any financial or legal advisors with respect to this transaction. We are in process of interviewing appropriate firms to assist us in this transaction. We will inform you of the firms that we ultimately hire as we move forward in this process.

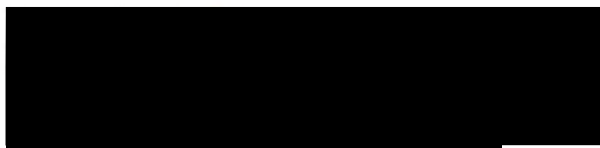
The following is a list of Prospect executives who are involved in the transaction and are available to discuss this non-binding indication of interest with you:

- George Pillari, Corporate Chief, Integration & Operations Improvement;
- Steve Aleman, Chief Financial Officer
- Frank Saidara, Vice President Corporate Development; and
- Andrew Finley, Corporate Director Mergers and Acquisitions

Please note that Prospect is flexible with respect to the structure of the transaction and its ultimate relationship with Verity. In event, Verity seeks an alternate structure or has other requirements, please let us know as we are confident that we will be able to structure a transaction that will meet Verity's needs.

This indication of interest is non-binding and is subject to the Confidentiality Agreement dated July 12, 2018 by and between the parties. If you have questions, please do not hesitate to contact me.

We look forward to working with you.



Frank Saidara
Vice President, Corporate Development

Appendix A

<i>PMH Propossal</i>				
<i>As of May 31, 2018</i>				
ASSETS	Seller	Acquired	Retained	Left Behind ⁽¹⁾
Cash and equivalents	\$ 58,648	\$ -	\$ 52,130	\$ 6,518
Net patient accounts receivable	239,495	230,061	-	9,434
Other accounts receivable	10,493	8,273	-	2,220
Inventory	24,715	24,189	-	526
Other Current Assets	98,885	88,072	-	10,813
Total current assets	432,236	350,595	52,130	29,511
Property and Equipment, net	266,116	260,983	-	5,133
Other Assets	21,722	19,444	-	2,278
Assets Limited as to Use	119,239	-	76,270	42,970
Total Assets	\$ 839,313	\$ 631,022	\$ 128,399	\$ 79,892
LIABILITIES				
Current Maturities of Long-Term Debt	\$ 6,410	\$ -	\$ 6,348	\$ 63
Accounts Payable	70,587	64,242	-	6,345
Accrued Liabilities & Other ⁽²⁾	297,094	187,930	-	109,164
Third-Party Liabilities	4,087	4,087	-	-
Total current liabilities	378,179	256,260	6,348	115,572
Long-Term Debt	580,189	-	540,189	40,000
Mortgage Payable	6,000	-	6,000	-
Workers Compensation	35,878	-	-	35,878
Pension Obligations	215,897	-	-	215,897
Deferred & Other Non-Current Liabilities	41,007	-	-	41,007
Total Liabilities	\$ 1,257,150	\$ 256,260	\$ 552,537	\$ 448,353
Net Equity	(417,837)			
Total Liabilities and Net Equity	\$ 839,313			
NET ASSETS ACQUIRED - BUYER		\$ 374,762		
NET LIABILITIES ASSUMED - SELLER			\$ (424,138)	

(1) "Left Behind" includes Assets/Liabilities associated with Marillac, the Medical Foundation, and certain Liabilities we assume will be eliminated through Bankruptcy.

(2) \$82 million Deferred Management Fee is being "Left Behind"